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BKI INVESTMENT COMPANY LIMITED

BKI Quarterly Report

Dividends and Franking Credits

In this issue:

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Welcome to the first issue of the BKI Quarterly Report. We will use these reports as an opportunity to communicate with shareholders to further improve the awareness of BKI.

BKI is a Listed Investment Company on the Australian Securities Exchange. Our aim is to create wealth for all BKI shareholders. BKI can offer investors capital growth and a growing fully franked dividend, through a diversified portfolio of Australian shares, trusts and interest bearing securities.

What is quite often not appreciated is the value of franking credits that are attached to dividends that BKI distributes. This issue of the BKI Quarterly Report will explain how franking credits can be very valuable to all Australian shareholders in various investment phases.

BKI receives dividends from its investments, highlighting that the 30% tax rate is already paid on most dividend income received from companies in which BKI invests.

The structure of BKI emphasizes:

i) the simplicity of owning shares in one LIC as opposed to many direct shares,

ii) the timing of dividends in regards to planning your taxable income for each financial year; and

iii) the diversification that an investment in BKI can provide.

Where does BKI's revenue come from?

Below is a step by step explanation of where BKI's revenues come from and how we pass through franking credits to shareholders.

- BKI's revenues come from dividends, distributions and interest from cash.
- 88% of BKI's revenues are fully franked dividends*, which simply means that the dividends received by BKI have already had the 30% tax rate paid by the companies in which it invests; e.g. CBA, NAB, WBC, ANZ, TLS, WOW, WES and BHP.
- From the revenue received, BKI pays its expenses (ASX fees, registry fees, staff costs etc). BKI's low expenses equate to a Management Expense Ratio (MER) of only 0.19%* which makes it one of the lowest cost, professionally managed equity products in the market.
- After BKI pays expenses it then pays tax. This is minimal due to the passing on of franking credits from the companies in which it invests. BKI effectively only pays tax on interest received from cash plus any unfranked dividends and trust distributions, less all expenses paid.
- BKI then pays out dividends from its Net Operating Result. Due to the passing on of franking credits and low expenses, BKI is able to pay out to its shareholders almost all revenues received from its investments.

"Do you know the only thing that gives me pleasure?

It's to see my dividends coming in..."

- John D. Rockefeller

Diversified market exposure and administration simplicity

An investment in BKI offers shareholders a diversified exposure to most sectors of the Australian sharemarket—BKI currently holds 58 companies in the portfolio. A BKI shareholder can easily monitor one shareholding as opposed to owning multiple shares directly. BKI shareholders also receive two dividends each year, generally paid in August and February. Therefore the shareholder can determine taxable income four months before 30 June and, unlike many managed funds and schemes, prepare their tax return promptly where a refund may be due.

Franking Credits, What are they actually worth?

Dividends and franking credits have the potential to increase after-tax returns of Australian Shareholders in all investment phases.

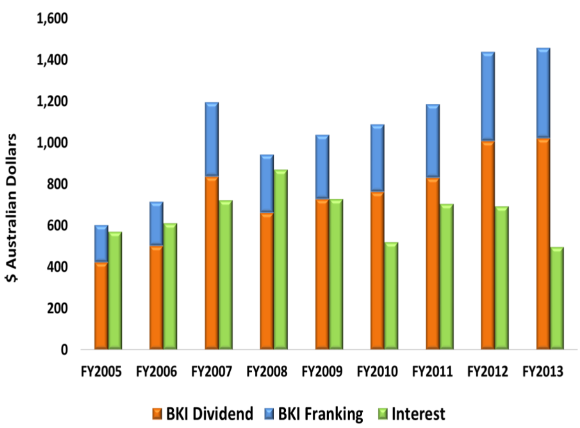
The table below assumes a $10,000 investment in BKI shares at $1.575** (a holding of 6,349 BKI shares). Dividend income is calculated using rolling 12 month dividends of 7.15 cents per share (includes FY2013 Final Ordinary Dividend of 3.40cps, FY2013 Interim Ordinary Dividend of 3.25cps and FY2013 Interim Special Dividend of 0.50cps).

As the table demonstrates, shareholders at any tax rate are able to benefit from franking credits attached to BKI dividends. For example, Shareholder A (an investor in pension phase who pays 0% tax) will receive all franking credits as a tax refund. This equates to a Post Tax Dividend Yield of 6.5% or $648.53 in after tax income. To highlight how valuable franking credits can be, if the same $10,000 was invested by Shareholder A in a Term Deposit with a rate of 3.75%pa, after tax income would be 42% lower at $375.00.

	Shareholder A	Shareholder B	Shareholder C	Shareholder D
Shareholders Marginal Tax Rate	0%	15%	30%	47%
Dividend Income	$453.97	$453.97	$453.97	$453.97
Franking Credits	$194.56	$194.56	$194.56	$194.56
Taxable Income	$648.53	$648.53	$648.53	$648.53
Grossed Up Dividend Yield	**6.5%**	**6.5%**	**6.5%**	**6.5%**
Gross Tax Payable	$0.00	$97.28	$194.56	$301.56
Less: Franking Credits	($194.56)	($194.56)	($194.56)	($194.56)
Tax Payable / (Refundable)	($194.56)	($97.28)	$0.00	$107.01
After Tax Income	$648.53	$551.25	$453.97	$346.96
Post Tax Dividend Yield	**6.5%**	**5.5%**	**4.5%**	**3.5%**
Interest Income on a $10k Term Deposit @ 3.75%pa	$375.00	$375.00	$375.00	$375.00
Tax Payable	$0.00	$56.25	$112.50	$174.38
After Tax Income	$375.00	$318.75	$262.50	$200.63
Post Tax Yield on Term Deposit	**3.8%**	**3.2%**	**2.6%**	**2.0%**
Cash Benefit of Fully Franked Dividend	**$273.53**	**$232.50**	**$191.47**	**$146.34**

Dividends for all seasons

The graph below shows that a shareholder who invested $10,000 in BKI shares upon listing in December 2003 would have received dividends of $1,019 in FY2013.



The franking credits would have enhanced this income by a further $437, bringing total income for this Shareholder to $1,456 last financial year. The same investment in a term deposit (based on the cash rate) would have returned $494 in pre tax interest last financial year (with no franking credits attached).

This example highlights the benefit of receiving a fully franked dividend in a falling interest rate environment.

BKI dividends are distributed bi-annually (generally in August and February). This enables the Shareholder to know exactly what their taxable income will be for that financial year, four months prior to 30 June.

Figures include reinvestment of dividends and cash. Ignores capital appreciation of BKI shares. Assumes tax rate of 30%.

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10 YEARS

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